STATE OF UTAH



JAN GRAHAM ATTORNEY GENERAL

JAMES SOPER

REED RICHARDS
Chief Deputy Asserted General

September 14, 2000

Steven O. Laing
State Superintendent of Public Instruction
Utah State Office of Education
250 East 500 South
Salt Lake City UT 84111

RE: Qualified Zone Academy Bonds and School Building Revolving Loan Account

Dear Mr. Laing:

In your letter dated August 1, 2000, you asked Attorney General Jan Graham for advice on Qualified Zone Academy Bonds ("QZAB") and the School Building Revolving Loan Account. (A copy of your August 1, 2000 letter, together with attachments thereto, is attached hereto and incorporated by reference.) In addition Pat O'Hara, Director of School Finance and Statistics, made an oral inquiry to our office regarding the same subjects. Inasmuch as John McCallister is the Assistant Attorney General ("AAG") assigned to represent the Utah State Office of Education, and Bryce Pettey is the AAG who handles bonding matters in the Attorney General's Office, we – John and Bryce – have been asked to respond to your letter.

A. The QZAB Program.

Attached to your August 1, 2000 letter was Issue Brief 00-7 ("Issue Brief 00-7") of the Federal Funds Information For States. As explained in that Issue Brief:

In 1997, Congress created [QZAB's] to help schools with low income populations save on interests costs associated with financing school construction. QZAB's cannot be used for new construction but may be used to renovate buildings, invest in equipment and up-to-date technology, develop challenging curricula, and training quality teachers. QZAB's were also designed to encourage schools and business to work together to enrich students' learning and to help students acquire the skills necessary to compete in a global economy. * * *

The original QZAB legislation made funds available for fiscal years 1998

and 1999. Since then, Congress and the President have extended the program through fiscal years 2000 and 2001. The program provides \$400 million per fiscal year for the QZAB program and the funds must be obligated within 2 years. This means that funds made available to states in fiscal year 1998 must be awarded by fiscal year 2000, while funds made available in fiscal year 2001 must be awarded by fiscal year 2003.

Since most schools normally fund large projects through debt mechanisms such as loans or bonds, schools must pay a substantial amount of interest on this debt. For schools serving low-income students, QZAB's reduce the burden of interest payment by giving financial institutions holding the bonds a tax credit in lieu of interest. The school district must still pay back the principal it originally borrowed but does not have to pay interest.

Each state is allotted an amount of money its schools may borrow using QZAB's. The allocation formula is based on state percentages of the national population of individuals with incomes below the poverty lines. States may develop their own procedures to award bond authority to qualified schools. A qualified school is one that is located in an Empowerment Zone or has at least 35 percent of its students eligible for free or reduced price school lunch. In addition, a qualified school must develop a partnership with a business that makes a contribution to the school worth at least 10% of the money borrowed under the QZAB program. Contributions can include cash; goods, including equipment and technology; services, including help developing curriculum or using technology; and internerships or field trips that help students learn outside the traditional classroom settings.

Utah has been notified that it has available approximately \$2 million each year under the QZAB program. This means that approximately \$2 million must be awarded before October 1, 2000, or that allotment will lapse and no longer be available for Utah schools. You have asked three questions with respect to the QZAB program in Utah:

Question No. 1: Is bonded indebtedness under the QZAB program similar in nature to customary bonded indebtedness, such that debt incurred under QZAB would apply against the 4% debt limit imposed on a school district by Article XIV Section 4 of the Utah Constitution?

Answer: Yes. Utah Constitution Article XIV Section 4 reads as follows:

* * * [N]o... school district... shall become indebted to an amount, including existing indebtedness, exceeding four per centum of the value of the taxable property therein, the value to be ascertained by the last assessment for State and

County purposes, previous to the incurring of such indebtedness; * * * provided, that no part of the indebtedness allowed in this section shall be incurred for other than strictly . . . school district purposes; * * *

Utah Constitution Article XVI Section 4 does not differentiate in any manner between different types of debt which a school district may incur. Therefore, the limitations of Article XIV Section 4 apply to QZAB's.

Question No. 2: Is bonded indebtedness under the QZAB program similar in nature to customary bonded indebtedness, such that debt incurred by a school district under QZAB would require voter approval as required under Article XIV Section 3 of the Utah Constitution?

Answer: Yes. Utah Constitution Article XIV Section 3 currently reads as follows:

No debt in excess of the taxes for the current year shall be created by any county.

.. or by any school district therein, ... unless the proposition to create such debt, shall have been submitted to a vote of such qualified electors as shall have paid a property tax therein, in the year preceding such election, and a majority of those voting thereon shall have voted in favor of incurring such debt.

Like Article XIV Section 4, Article XIV Section 3, makes no distinction between the different

No debt issued by a county, city, town, school district, or other political subdivision of this state and directly payable from and secured by ad valorem property taxes levied by the issuer of the debt may be created in excess of the taxes for the current year unless the proposition to create the debt has been submitted to a vote of qualified voters at the time and in the manner provided by statute, and a majority of those voting thereon has voted in favor of incurring the

Court cases have held, however, that where bonds are issued to pay for the purchase or construction of private property, and payment on the bonds is to be made exclusively from the revenue derived from the property, the limitations in Utah Const. Art. XIV, Sections 3 and 4, do not apply (the "special fund doctrine"). See, e.g., Utah Power & Light Co. v. Provo City, 73 P.2d 1191 (Utah 1937), cert. denied, 305 U.S. 628 (1938).

² In the upcoming general election to be held on November 7, 2000, electors will vote on language approved in SJR 5, Section 16 (2000 Gen. Sess.), which would amend Article XIV, Section 3 to read as follows:

kinds of debt a school district might incur³. The only distinction mentioned in Article XIV Section 3 is debt that would not exceed the taxes for the current year. Assuming the debt incurred through a QZAB program loan would exceed the taxes for the current year, the provisions of Article XIV Section 3 requiring that the incurring of such debt be submitted to the electorate would apply.

Question No. 3: Is bonded indebtedness under the QZAB program similar in nature to customary bonded indebtedness, such that debt incurred under QZAB could be retired with proceeds from a school's capital outlay and/or debt service tax levies?

Answer: Yes. Utah Code Ann. §53A-16-107 provides, relevant part:

(1) (a) A local school board may levy a tax not to exceed .0024 per dollar of taxable value for debt service and capital outlay.

(b) Each local school board may utilize the proceeds of a maximum of .0002 per dollar of taxable value of its annual capital outlay levy for the maintenance of school plants in its school district.

(2) A board that uses the option provided under Subsection (1)(b) must do the

(a) maintain the same level of expenditure for maintenance in the current year as it did in the preceding year, plus the annual average percentage increase applied to the maintenance and operation budget for the current year, and

(b) identify the expenditure of capital outlay funds for maintenance by a district project number to ensure that the funds were expended in the manner intended.

According to Issue Brief 00-7, while QZAB's cannot be used for new construction, they may be used to renovate buildings. While the term "capital outlay", as used in §53A-16-107, is nowhere defined, use of funds to renovate a building would clearly be use of funds for a "capital outlay" as that term is commonly used, and therefore debt service and capital outlay levies could be used to repay QZAB bonds issued for those purposes. However, Issue Brief 00-7 also says that QZAB bonds can be used to invest in equipment and up-to-date technology, develop challenging curricula and train quality teachers. None of those uses would be for the purposes of a "capital outlay", again as that term is commonly used. However, we have been unable to find any reference in Title 53A or elsewhere that limits the purposes for which a local school board may issue debt except for the provisions in Article XIV Section 4 that the debt allowed in that section must be for school district purposes. It therefore follows that a local school board may issue debt to "invest in equipment and up-to-date technology, develop challenging curricula and train quality teachers." That being the case, the debt service and capital outlay levy may also be

³ See footnote 1.

used to pay debt service on QZAB bonds issued for purposes other than for the renovation of buildings.

B. The School Building Revolving Account.

In addition to inquiring about the QZAB program, you make inquiry as to the School Building Revolving Account ("Revolving Account") found at §53A-21-104. As explained in your letter, that fund was established by statute several years ago for the purpose of assisting school districts with building construction and renovation and was initially funded with an appropriation of \$10 million. Funds from this account are loaned to school districts at the discretion of a committee convened by the state superintendent of public instruction. Payment schedules are from 5 to 10 years and the loans are interest-bearing. Given this background, you asked three questions with respect to the Revolving Account that are similar to the questions you asked with respect to the QZAB's.

Question No. 4: Is indebtedness under the Revolving Account similar in nature to bonded indebtedness, such that debt incurred under the Revolving Account would apply against the 4% debt limit imposed on a school district by Article XIV of Section 4 of the Utah Constitution?

Answer: Yes. As your letter suggests, Utah Code Ann. §53A-21-104(2) requires that any loans received from the revolving fund be counted against a school board's debt limit. That section provides, "Monies received by a school district from the School Building Revolving Account may not exceed the district's bonding limit minus its outstanding bonds." The term "bonding limit" in §53A-21-104(2) is not defined therein, nor is it defined anywhere else in Title 53A. It would seem that the term was intended to reference the limitations placed upon school districts by Utah Constitution Article XIV Section 4. That constitutional provision, as noted above, does not differentiate in any way between the types of debt a school district may incur. It is therefore our view that Article XIV Section 4 already applies to debt a school district might incur through a loan from the revolving fund; the language in §53A-21-104(2) only serves to emphasize the limitations already set forth in the Utah Constitution.

Question No. 5: Is indebtedness under the Revolving Account similar in nature to bonded indebtedness, such that debt incurred by a school district under the Revolving Account would require voter approval as required under Article XIV Section 3 of the Utah Constitution?

Answer: Yes. Again as stated above, Article XIV Section 3 makes no distinction between the types of debt incurred by a school district, nor as to the lender of those funds. Whether funds are borrowed through a public sale of general obligation bonds, a private placement of debt instruments, or a loan from a state or other governmental entity, debt is debt. The restrictions of Article XIV Section 3 therefore apply.

Question No. 6: Is the indebtedness under the Revolving Account similar in nature to bonded indebtedness, such that debt incurred under the Revolving Account could be retired with proceeds from a school district's capital outlay and debt service levies?

Answer: Yes. Your letter states that §53A-21-104(3)(c) seems to say yes. That may or may not be the case. Subsection 53A-21-104(3) provides as follows:

- (3) In order to receive monies from the account, a school district must do the following:
- (a) levy a tax of at least .0024 for capital outlay and debt service;
- (b) contract with the state superintendent of public instruction to repay the monies, with interest at a rate established by the state superintendent, within five years of their receipt, using future state building monies or local revenues or both:
- (c) levy sufficient ad valorem taxes under Section 11-14-19 to guarantee annual loan repayments, unless the state superintendent of public instruction alters the payment schedule to improve a hardship situation; and
- (d) meet any other condition established by the State Board of Education pertinent to the loan.

Subsection 53A-21-104(3)(c) does not seem to relate directly to the question of whether capital outlay and debt service funds levies can be used to repay loans received from the Revolving Account. Nonetheless, as stated above, the purposes for which debt may be incurred by a school district are not limited in any way in Title 53A or elsewhere, as long as the debt is incurred for school district purposes as required by Article XIV Section 4 of the Utah Constitution. Nor is there any limitation found anywhere on the types of debt for which the "debt service" levy may be used. The capital outlay and debt service levy may therefore be used to service debt incurred through a loan from the Revolving Account.

Should you have any further questions, please let us know.

Singerely,

John A. McCallister

Assistant Attorney General

Bryce H. Pettey

Assistant Attorney General



H STATE OFFICE F EDUCATION D East 500 South it Lake City, Utah R4111

ven O. Laing, Ed.D. re Superintendent Public Instruction

August 1, 2000

Janet C. Graham Attorney General 236 State Capitol Salt Lake City, Utah 84114

Subject: Qualified Zone Academy Bonds and School Building Revolving Loan Account

Dear Ms. Graham:

am writing regarding the federal government's Qualified Zone Academy Bonds (QZAB) and the Utah State Office of Education's "School Building Revolving Account." The State Office of Education has recently been established as the fiscal agent for the QZAB program in Utah and has been involved in the revolving loan program for some years. While evaluating school district applications for participation in the QZAB program, several questions arose that actually relate to both programs. To more fully inform the committee evaluating these applications, we are seeking the advice of the State Treasurer, bond counsel, and the Attorney General in an effort to answer those questions. I have attached some background information relating to the QZAB program. The first three questions relate to the QZAB program. Questions four, five, and six are similar to the first three, but relate to the Revolving Loan Account.

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Question No. 1:

is bonded indebtedness under the QZAB program similar in nature to customary bonded indebtedness, such that debt incurred under QZAB would apply against the four percent debt limit imposed on a school district by Article XIV Section 4 of the Utah Constitution?

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is bonded indebtedness under the QZAB program similar in nature to customary bonded indebtedness, such that debt incurred by a school district under QZAB would require voter approval as required under Article XIV Section 3 of the Utah Constitution?

Question No. 3:

Is bonded indebtedness under the QZAB program similar in nature to customary bonded indebtedness, such that debt incurred under QZAB could be retired with proceeds from a school district's capital outlay and/or debt service tax levies?

Authority for the School Building Revolving Account can be found at 53A-21-104. It was established by statute several years ago for the purpose of assisting school districts with building construction and renovation and was initially funded with an appropriation of \$10 million. Funds from this account are loaned to school districts at the direction of a committee convened by the State Superintendent of Public Instruction. Repayment schedules vary from five to 10 years and State Superintendent of Siven this background, I have similar questions for the Revolving Account:

Question No. 4:

Is indebtedness under the Revolving Account similar in nature to bonded indebtedness, such that debt incurred under the Revolving Account would apply against the four percent debt limit imposed on a school district by Article XIV Section 4 of the Utah Constitution? (53A-21-104(2) seems to say yes).

Question No. 5:

Is indebtedness under the Revolving Account similar in nature to bonded indebtedness, such that debt incurred by a school district under the Revolving Account would require voter approval as required under Article XIV Section 3 of the Utah Constitution?

Question No. 6:

Is indebtedness under the Revolving Account similar in nature to bonded indebtedness, such that debt incurred under the Revolving Account could be retired with proceeds from a school district's capital outlay and debt service tax levies? (53A-21-104(3)(c) seems to say yes).

I hope that I've provided sufficient background information to enable you to provide opinions for these questions. If you need further information, please let me know. The school districts involved in the QZAB program have made arrangements with private industrial partners for the necessary matching funds and would like to move forward while commitments are fresh and enthusiasm is high. We appreciate your willingness to consider these questions for us.

Sincerely,

Steven O. Lairg Ed.D. ()
State Superintendent of Public Instruction

MEMORANDUM

TO:

District Business Administrators

FROM:

Pat O'Hara, Director

School Finance & Statistics

DATE:

April 6, 2000

SUBJECT:

QZAB Program

At the March UASBO conference we briefly introduced the federally-funded interest-free loan program known as Qualified Zone Academy Bonds (QZAB). Subsequent to the conference, we e-mailed additional information to district business administrators regarding the qualifying criteria. A few school districts have also discussed the program with officials from the banking and finance industry. We have accumulated additional information from the federal agency responsible for implementation of the program and are now prepared to move forward with interested school districts. You will find an application form accompanying this memorandum.

A brief review of the QZAB program might prove useful. This is a loan program funded by a federal appropriation of some \$400 Million. Utah's unused share has accumulated over three years and now stands at \$5,591,000. Assuming continued funding by Congress, Utah's annual authorization hereafter is expected to be approximately \$2 Million. Funds are loaned interest free to the borrower under a customary general obligation bond and lenders realize their interest by way of tax credits. Please refer to Larry Newton's e-mails of March 23, 24, and 27 for additional background. You will recall that (a) loans are restricted to schools located in federally-designated enterprise zones or in which at least 35% of students qualify for free or reduced-price lunch, (b) a district must have public authorization for this debt, (c) a 10% match (in goods or services) must be provided by a corporate partner, (d) the debt will count against the district's debt ceiling, and (e) according to the State Treasurer, this debt qualifies for coverage under the Utah Bond Guaranty Act. You will also recall that QZAB proceeds can be used for building renovation, equipment, technology, curricula, and staff development.

In some states this has been a popular program with demand exceeding available funds. Those states have adopted various methods for apportioning available loan authority. Since we are unsure at this point what the level of interest in this program might be in Utah, we have not established any participation limits. Should interest be high, as evidenced by a large number of applications or applications for large amounts of loan authority, a committee would be appointed to apportion the total loan authority in an equitable manner. Please be advised that \$1,576,000 (the 1998 appropriation for Utah) will lapse in October if it is not committed, leaving total available loan authority at \$4,015,000.

We understand that some interested districts might have to seek additional debt authority. If this is the case in your district, and you intend to pursue it, please advise me of your plans as soon as possible and follow that up by filing your application at your earliest convenience. This will allow us to appoint a committee if necessary and get the program under way. If we can provide additional information, contact me at 538-7665 or Larry Newton at 538-7668.



ISSUE BRIEF 00-7

Qualified Zone Academy Bonds: How Do They Work? March 29, 2000

Executive Summary

In 1997, Congress created Qualified Zone Academy Bonds (QZABs) to help schools with low-income populations save on interest costs associated with financing school construction. QZABs cannot be used for new construction but may be used to renovate buildings, invest in equipment and up-to-date technology, develop challenging curricula, and train quality teachers. QZABs were also designed to encourage schools and businesses to work together to enrich students' learning and help students acquire the skills necessary to compete in a global economy. At least 16 states are currently using QZABs and four additional states are developing QZAB applications. This Issue Brief will outline the QZAB program and provide individual state allotment amounts in Table 1.

low Does the Program Work?

The original QZAB legislation made funds available for fiscal years 1998 and 1999. Since then, Congress and the President have extended the program through fiscal years 2000 and 2001. The program provides \$400 million per fiscal year for the QZAB program and the funds must be obligated within two years. This means that funds made available to states in fiscal year 1998 must be awarded by fiscal year 2000, while funds made available in fiscal year 2001 must be awarded by fiscal year 2003.

Since most schools normally fund large projects through debt mechanisms such as loans or bonds, schools must pay a substantial amount of interest on this debt. For schools serving low-income students, QZABs reduce the burden of interest payments by giving financial institutions holding the bonds a tax credit in lieu of interest. The school district still must pay back the principal it originally borrowed but does not have to pay interest.

Each state is allotted an amount of money its schools may borrow using QZABs. The allocation formula is based on state percentages of the national population of individuals with incomes below the poverty line. States may develop their own procedures to award bond authority to qualified schools. A qualified school is one that is located within an Empowerment Zone or has at least 35 percent of its students eligible for free or reduced price school lunch. In addition, a qualified school must develop a partnership with a business that makes a contribution to the school worth at least 10 percent of the money borrowed under the QZAB program. Contributions can include cash; goods, including equipment and technology; services, including help developing curriculum or using technology; and internships or field trips that help students learn outside the traditional classroom setting.